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[JOINT COMMITTEE PRINT]

SUMMARY OF REVENUE PROVISIONS IN PRESIDENT BUSH'S FISCAL YEAR 1990 BUDGET PROPOSAL

PREPARED BY THE STAFF

OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

This pamphlet,[1] prepared by the staff of the Joint Committee on Taxation, provides a summary of the revenue provisions included in President Bush's budget proposal for fiscal year 1990, submitted to the Congress on February 9, 1989.[2]

The first part of the pamphlet is a summary of the revenue proposals contained in President Bush's budget proposal (referred to as the "President's Budget Proposal"), including present law and a reference to any recent prior Congressional action on the topic and whether the proposal was also included in President Reagan's fiscal year 1989 or 1990 budget proposals.[3] The second part of the pamphlet presents the Administration's (Treasury Department) estimates of the revenue effects of the proposals, as they affect budget receipts.

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[1] This pamphlet may be cited as follows: Joint Committee on Taxation, *Summary of Revenue Provisions in President Bush's Budget Proposal for Fiscal Year 1990* (JCS-6-89), March 3, 1989.

[2] See Treasury Department, *General Explanations of the President's Budget Proposals Affecting Receipts*, February 1989; The White House, *Building a Better America*, February 9, 1989.

[3] *Budget of the United States Government, Fiscal Year 1989*; *Budget of the United States Government, Fiscal Year 1990.*

I. SUMMARY OF REVENUE PROVISIONS

A. Tax Provisions

1. Capital Gains Tax Rate Reduction for Individuals

Present Law

Under present law, net gain from the sale or exchange of capital assets is taxed at the same rates as ordinary income. Individuals with a net capital loss generally may deduct up to $3,000 of the loss each year against ordinary income. Net capital losses in excess of the $3,000 limit may be carried forward indefinitely.

President's Budget Proposal

The President's budget proposal would allow individuals an exclusion of 45 percent of the gain realized upon the disposition of qualified capital assets. Further, the maximum tax rate applicable to any gains on qualified assets would be 15 percent. The exclusion would not be a preference for purposes of the alternative minimum tax. Taxpayers with gain on qualified assets would be able to exclude 100 percent of the gain, if the taxpayer's adjusted gross income (calculated including 55 percent of the gain) is less than $20,000 ($10,000 for single taxpayers or married taxpayers filing separately). Taxpayers with an adjusted gross income less than $20,000 but who are subject to the alternative minimum tax would not be eligible for the 100 percent exclusion.

Qualified capital assets generally would be capital assets as defined under present law other than depreciable, depletable, and amortizable property used in the taxpayer's trade or business. Collectibles would not be treated as qualified assets. The special section 1231 assets, *i.e.*, certain interests in timber, coal, iron ore, livestock, and unharvested crops, would not be treated as qualified assets.

In addition, to be a qualified asset, the taxpayer must satisfy a holding period requirement. The asset must have been held for more than 12 months if the asset is sold in 1989, 1990, 1991, or 1992; for more than 24 months if the asset is sold in 1993 or 1994; and for more than 36 months if the asset is sold in any year after 1994.

The proposal would be effective for assets sold on or after July 1, 1989.

Prior Action

The Tax Reform Act of 1986 repealed the prior law exclusion of 60 percent of long-term capital gains (assets held for greater than 6 months), effective January 1, 1987.

2. Child Tax Credit and Refundable Child and Dependent Care Tax Credit

Present Law

Earned income tax credit

Under present law, low-income workers with minor dependents are eligible for a refundable income tax credit of up to 14 percent of the first $6,500 of earned income for 1989 (sec. 32). The maximum amount of the credit is $910. The credit is reduced by an amount equal to 10 percent of the excess of the greater of (a) adjusted gross income (AGI) or (b) earned income over $10,240. The credit is not available to taxpayers with AGI over $19,340. The maximum amount of earnings with respect to which the credit may be claimed and the income level at which the phaseout of the credit begins are adjusted for inflation.

Earned income eligible for the credit includes wages, salaries, tips and other employee compensation, plus the amount of the taxpayer's net earnings from self-employment. Eligible individuals may utilize an advance payment system to receive the benefit of the credit in their paychecks.

Child and dependent care credit

Under present law, a nonrefundable income tax credit is allowed for up to 30 percent of a limited dollar amount of employment-related child or dependent care expenses (sec. 21). Eligible employment-related expenses are limited to $2,400 in the case of one qualifying individual ($4,800 in the case of two or more qualifying individuals). The 30-percent credit rate is reduced by one percentage point for each $2,000 (or fraction thereof) of the taxpayer's adjusted gross income (AGI) between $10,000 and $28,000. The credit rate is 20 percent for taxpayers with AGI in excess of $28,000.

The term "qualifying individual" means (1) a dependent of the taxpayer who is under age 13 and with respect to whom the taxpayer is entitled to claim a dependent exemption, (2) a dependent of the taxpayer who is physically or mentally incapable of caring for himself, or (3) a spouse of the taxpayer if the spouse is physically or mentally incapable of caring for himself.

Under present law, the dollar amount of expenses eligible for the dependent care credit of any taxpayer is reduced dollar for dollar by the amount of expenses excludable from that taxpayer's income under the dependent care exclusion (sec. 129).

President's Budget Proposal

Proposed child tax credit

Under the President's budget proposal, low-income families with at least one working individual would be entitled to claim a new refundable tax credit of up to $1,000 for each dependent child under age four. For each child under the age of four, families could claim a credit equal to 14 percent of earned income, with a maximum credit equal to $1,000 per child. Initially, the credit would be reduced by an amount equal to (1) 20 percent times the number of such children multiplied by (2) the excess of the greater of (a) ad-

justed gross income (AGI) or (b) earned income over $8,000. The credit would not be available to families with AGI or earned income greater than $13,000. In subsequent years, both the starting and end-points of the phaseout range would be increased by $1,000 increments. In 1994, the credit would phaseout between $15,000 and $20,000.

The credit would be effective for taxable years beginning on or after January 1, 1990. Families would have the option of receiving the tax benefit through an advance payment system similar to the earned income tax credit. Under such advance payment system, the individual would file a claim with the individual's employer to receive the credit in the form of reduced income tax withholding. In the event that the amount of the credit exceeds total withholding, then the employer would make a payment to the employee in conjunction with the regular employee paycheck. The employer would reduce the amount of withholding it submits to the Treasury by the amount of the payment made to the employee.

Refundable child and dependent care credit

Under the President's budget proposal, the existing child and dependent care tax credit would be made refundable. Families could not claim both the new child credit and the child and dependent care credit with respect to the same child, but could choose the larger of the two credits. The refundable child and dependent care credit would be effective for taxable years beginning on or after January 1, 1990.

3. Adoption Expense Deduction

Present Law

The Tax Reform Act of 1986 (the "1986 Act") repealed the deduction for adoption expenses associated with special needs children, effective for taxable years beginning on or after January 1, 1987. Under prior law, a deduction of up to $1,500 of expenses associated with the adoption of special needs children was allowed. The 1986 Act provided for a new outlay program under the existing Adoption Assistance Program to reimburse expenses associated with the adoption process of these children. The group of children covered under the outlay program is somewhat broader than the group covered by the prior deduction. Aid to Families with Dependent Children (AFDC) and Title IV-E Foster Care assistance outlay program provides assistance for adoption expenses for these special needs children as well as special needs children in private and State-only programs.

One component of the Adoption Assistance Program requires States to reimburse certain costs incurred for special needs children. The Federal Government shares 50 percent of these costs up to a maximum Federal share of $1,000 per child. Reimbursable expenses include those associated directly with the adoption process such as legal costs, social service review, and transportation costs.

President's Budget Proposal

The President's budget proposal would permit an itemized deduction for certain incurred expenses associated with the adoption of special needs children up to a maximum of $3,000 per child. Eligible expenses would be limited to those: (1) directly associated with the adoption process and (2) that are of a type eligible for reimbursement under the Adoption Assistance Program. These include court costs, legal expenses, social service review, and transportation costs. A deduction of up to $3,000 would be allowed for eligible expenses regardless of the level of reimbursement allowed under the Adoption Assistance Program. Expenses which were deducted and reimbursed would be included in income in the year in which the reimbursement occurred.

The proposal also clarifies that all reimbursements are includible in income to the recipient unless deductible under this provision.

The provision would be effective for calendar years after December 31, 1989.

4. Enterprise Zone Tax Incentives

Present Law

The Internal Revenue Code does not contain general rules that target specific geographic areas for special tax treatment. Existing general tax provisions, however, may provide an incentive for economic development in economically distressed areas. Such provisions include: (1) qualified mortgage bond provisions which define targeted areas for the purpose of promoting housing development within economically distressed areas; (2) the targeted jobs tax credit, which provides a tax credit for a portion of wage payments made to certain disadvantaged employees; (3) a tax credit for certain investment in low-income housing; (4) a tax credit for rehabilitation of certain structures; and (5) provisions which permit State and local governments to issue a limited amount of tax-exempt private activity bonds to finance certain business ventures.

President's Budget Proposal

The President's budget proposes that up to 70 enterprise zones would be selected between 1990 and 1993. Within these zones, selected Federal employment and investment tax credits would be offered, in conjunction with Federal, State, and local regulatory relief. Under the proposal, the extent of the tax subsidies would vary, with larger subsidies in the early years that would decline over time.

Prior Action

During the 100th Congress, the Senate Finance Subcommittee on Taxation and Debt Management held a hearing on S. 788 and S. 983, which would provide special tax incentives for certain designated Indian enterprise zones and rural enterprise zones. The Housing and Community Development Act of 1987 authorizes the establishment of 100 enterprise zones. The Act establishes the cri-

teria to be used in nominating and selecting areas to be designated as enterprise zones, but does not provide any tax incentives.

5. Tax Credit for Qualified Research Expenditures

Present Law

A 20 percent tax credit is allowed for the amount of qualified research expenses paid or incurred by a taxpayer during a taxable year that exceeds the base period amount. That amount generally is the average amount of qualified research expenses incurred during the preceding three taxable years. Qualified research expenses consist of: (1) in-house expenses of the taxpayer for research wages and supplies used in research; (2) certain time-sharing costs for computer use in research; and (3) 65 percent of amounts paid by the taxpayer for contract research conducted on the taxpayer's behalf.

In addition, the 20-percent tax credit also applies to the *excess* of (1) 100 percent of corporate cash expenditures (including grants or contributions) paid for university basic research *over* (2) the sum of (a) the greater of two fixed research floors plus (b) an amount reflecting any decrease in nonresearch giving to universities by the corporation as compared to such giving during a fixed base period, as adjusted for inflation.

Deductions for qualified research expenses allowed to a taxpayer under sec. 174 are reduced by an amount equal to 50 percent of the research credit determined for the year.

President's Budget Proposal

The President's proposal would retain the incremental feature of the present credit and its 20-percent rate, but would make the credit permanent and modify the calculation of the base amount. The new base would be a fixed historical base equal to 102 percent of the average of the firm's qualified research expenses for the years 1983 through 1987, indexed to growth in the gross national product (GNP). Firms would have the option of claiming a separate credit equal to 7 percent of the current year's qualified research expenses in excess of 75 percent of this new base. Deductions under sec. 174 in a taxable year would be reduced by the full amount of the credit determined for the year. The trade or business test also would be liberalized to allow new firms and firms entering new lines of business to claim the credit.

Prior Action

The credit for qualified research expenses was enacted initially in the Economic Recovery Tax Act of 1981 as a credit equal to 25 percent of the excess of qualified research expenses in the current taxable year over the average of qualified research expenses in the prior three taxable years. The credit was modified in the Tax Reform Act of 1986 which (1) extended the research credit through December 31, 1988; (2) reduced the credit rate to 20 percent; (3) tightened the definition of research expenditures eligible for the credit; and (4) modified the university basic research credit.

The Technical and Miscellaneous Revenue Act of 1988 extended the credit for one additional year through December 31, 1989. The Act also reduced the deduction allowed under sec. 174 for qualified research expenses by an amount equal to 50 percent of the research credit determined for the year.

A proposal to make the credit permanent was included in President Reagan's budget submissions for fiscal years 1989 and 1990.

6. Allocation and Apportionment of Research Expenses

Present Law

Computation of the foreign tax credit requires the taxpayer to distinguish between taxable income from U.S. sources and taxable income from foreign sources, and thus to allocate and apportion deductions among items of U.S. source and foreign source gross income. Treasury regulations prescribe a detailed method for allocating and apportioning research and experimental (R&D) expenses for this purpose, among others.

Effective for taxable years beginning after August 13, 1981, and on or before August 1, 1987, as well as for a taxpayer's first taxable year beginning after August 1, 1987, the R&D allocation regulation was in part suspended (for purposes of determining the source of taxable income) by a succession of statutes: the Economic Recovery Tax Act of 1981 (ERTA), the Deficit Reduction Act of 1984 (DEFRA), the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), the Tax Reform Act of 1986 (TRA), and the Technical and Miscellaneous Revenue Act of 1988 (TAMRA). In taxable years governed by ERTA, DEFRA, and COBRA, all U.S.-incurred R&D expenses were allocated to U.S. source income. In taxable years governed by TRA, 50 percent of such expenses (other than amounts incurred to meet certain legal requirements, and thus allocable to one geographical source) were allocated to U.S. source income, with the remainder allocated and apportioned either on the basis of sales or gross income.

Expenses incurred during the taxable year governed by TAMRA (for any taxpayer, its first taxable year beginning after August 1, 1987) were treated in one of two alternative ways depending upon whether the expenses were in effect deemed to have been incurred in the first four months of the year, or incurred instead during the remaining eight or fewer months of the year (for these purposes total expenses for the year were deemed to be incurred evenly throughout the year). For expenses falling into the first category (other than amounts incurred to meet certain legal requirements, and thus allocable to one geographical source), 64 percent of U.S.-incurred R&D expenses were allocated to U.S. source income, 64 percent of foreign-incurred R&D expenses were allocated to foreign source income, and the remainder of R&D expenses were allocated and apportioned either on the basis of sales or gross income, but subject to the condition that if income-based apportionment was used, the amount apportioned to foreign source income could be no less than 30 percent of the amount that would have been apportioned to foreign source income had the sales method been used. For expenses deemed paid or incurred during the remaining eight

(or fewer) months of the year governed by TAMRA, the R&D allocation regulation applied.

President's Budget Proposal

Under the President's budget proposal, taxpayers would be permitted to allocate 67 percent of expenses for R&D conducted in the United States to U.S. source income. The remainder of such expenses would be apportioned on the basis of either gross sales or gross income, with no limitation on the amount apportioned to U.S. source income using the gross income method.

The proposal would apply retroactively beginning with that portion of R&D expenses which were paid or incurred in the taxable year covered by TAMRA and which were not eligible for allocation and apportionment under TAMRA's 64-percent automatic allocation rules. For example, assume that a taxpayer has a taxable beginning January 1, 1988, and ending December 31, 1988, and that this is the taxpayer's first taxable year beginning after August 1, 1987. Under the proposal, this taxpayer would apply TAMRA's 64-percent automatic allocation rules to one-third of its 1988 R&D expenses, and would apply the 67-percent automatic allocation rules of the President's proposal to the other two-thirds of 1988 R&D expenses. The proposal would also apply to all R&D expenses paid or incurred in 1989 and subsequent taxable years.

Prior Action

In COBRA, the 99th Congress extended by one year the ERTA/DEFRA modification of the R&D regulation. In TRA, the same Congress enacted the temporary allocation rule that generally allowed taxpayers to allocate at least 50 percent of domestic R&D expense to U.S. source income.

At a hearing before a subcommittee of the Senate Finance Committee on April 3, 1987, during the 100th Congress, the Administration testified in favor of a proposal similar to the R&D allocation proposal now in the President's budget for fiscal year 1990. The Administration's 1987 proposal was included in H.R. 3545, the Omnibus Budget Reconciliation Act of 1987 (OBRA), as passed by the House. The proposal also was included in the October 1987 budget reconciliation submission of the Senate Finance Committee to the Senate Budget Committee. The proposal was not included in the conference agreement on OBRA.

Permanent statutory R&D allocation rules similar to those in H.R. 3545 as passed by the House in 1987 were included in the President's budget proposal for fiscal year 1989. The Miscellaneous Revenue Act of 1988, H.R. 4333, as passed by the House in August 1988, included statutory modifications to the R&D allocation regulation, which modifications were to be in effect from the expiration of the TRA R&D allocation rules through taxable years beginning before 1991. The substantive provisions of H.R. 4333 as passed by the House would have been similar to the proposal included in H.R. 3545 with three primary modifications: (1) 64 percent of U.S.-incurred R&D expenses would be allocated to U.S. source income, rather than 67 percent; (2) 64 percent of foreign-incurred R&D expenses would be allocated to foreign source income; (3) if income-

based apportionment was used, the amount apportioned to foreign source income could be no less than 30 percent of the amount that would have been apportioned to foreign source income had the sales method been used.

The Senate substitute for H.R. 4333 passed on October 11, 1988 included substantive R&D allocation rules like those in the House-passed bill, but under the Senate bill the statutory rules expired, in effect, after the first four months of the taxpayer's first taxable year beginning after August 1, 1987 (treating R&D expenses for the entire year as if incurred ratably throughout the year). In conference, the Senate version was adopted and became part of TAMRA.

The President's current proposal on R&D allocation rules was also included in President Reagan's budget for fiscal year 1990.

7. Energy Tax Provisions

a. Tax credits for oil and gas exploration and tertiary recovery

Present Law

New oil and gas reserves are typically identified by exploratory drilling (i.e., drilling in a property not previously drilled and not located next to another producing property). Present law does not provide any credit for exploratory drilling. However, intangible drilling and development costs ("IDCs"), including IDCs attributable to exploratory drilling, generally may be deducted as an expense.

Tertiary enhanced recovery techniques increase available reserves by producing oil and gas that cannot be recovered economically through conventional recovery techniques. Present law does not provide any credit for projects using these techniques. However, certain tertiary injectant expenses may be deducted in the year paid or incurred.

President's Budget Proposal

The President's budget proposal would provide a 10-percent tax credit for the first $10 million (per year per company) of IDCs attributable to exploratory drilling. A 5-percent credit would be allowed for the balance of the IDCs attributable to exploratory drilling.

In addition, the President's budget proposal would provide a 10-percent tax credit for all capital expenditures on projects that represent the initial application of tertiary enhanced recovery techniques to a property.

These tax credits could be applied against both the regular tax and the alternative minimum tax. However, these credits, in conjunction with all other credits and net operating loss carryforwards, could not eliminate more than 80 percent of the tentative minimum tax in any year. Unused credits could be carried forward.

The tax credits would be phased out if the average daily U.S. wellhead price of oil is at or above $21 per barrel for a calendar year.

The credits would be effective on January 1, 1990.

b. Modification of oil and gas percentage depletion rules

Present Law

Under present law, independent oil producers and royalty owners (but not integrated oil companies) recover certain costs incurred prior to drilling an oil- or gas-producing property using the higher of cost or percentage depletion. Under percentage depletion, 15 percent of the taxpayer's gross income from an oil- or gas-producing property is allowed as a deduction in each taxable year. The amount deducted may not exceed 50 percent of the taxable income from the property for the taxable year, computed without regard to the depletion deduction (the "net income limitation"). Additionally, the deduction for all oil and gas properties may not exceed 65 percent of the taxpayer's overall taxable income (determined with certain adjustments).

In addition, percentage depletion for oil and gas properties for independent producers and royalty owners is limited to 1,000 barrels of average daily domestic crude oil production (or an equivalent amount of natural gas). If an interest in a proven oil or gas property is transferred after 1974, production from that interest generally does not qualify for percentage depletion.

President's Budget Proposal

The President's budget proposal would increase the net income limitation from 50 percent to 100 percent.

In addition, the President's budget proposal would repeal the percentage depletion anti-transfer rules.

The proposal would be effective on January 1, 1990.

Prior Action

President Reagan's budget proposals for fiscal years 1989 and 1990 contained the same recommendations.

c. Modification of tax preference for IDCs in the alternative minimum tax

Under present law, domestic IDCs generally may either be currently expensed or else may be capitalized and recovered through depletion or depreciation deductions (as appropriate), at the election of the operator. In general, IDCs include expenditures by the property owner incident to and necessary for the drilling and the preparation of wells for the production of oil and gas (or geothermal energy) which are neither for the purchase of tangible property nor part of the acquisition price of an interest in the property. IDCs include amounts paid for labor, fuel, repairs, and site preparation. Costs that do not qualify as IDCs must be capitalized and recovered through depreciation or depletion.

Taxpayers are subject to an alternative minimum tax which is payable, in addition to all other tax liabilities, to the extent it exceeds the taxpayer's regular tax. The tax is calculated with respect to alternative minimum taxable income, which generally is the taxpayer's taxable income, as increased or decreased by certain adjustments and preferences. IDC deductions on successful oil and gas

wells are a tax preference item for this purpose, to the extent that the taxpayer's "excess IDCs" exceed 65 percent of the taxpayer's income from oil and gas properties. Excess IDCs are defined generally as (1) IDC deductions (attributable to successful wells) for the taxable year, minus (2) the amount that would have been deductible in that year had the IDCs been capitalized and recovered over a 10-year, straight-line amortization period. At the election of the operator, the cost depletion method may be substituted for the 10-year amortization schedule in determining the amount of the tax preference.

President's Budget Proposal

The President's budget proposal would eliminate 80 percent of the present law minimum tax preference item for IDCs attributable to exploratory drilling incurred by independent producers.[4]

The proposal would be effective on January 1, 1990.

8. Extension of Medicare Payroll Tax to All State and Local Government Employees

Present Law

Prior to enactment of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), State and local government employees were covered under the Medicare system only if the State and the Secretary of Health and Human Services entered into a voluntary agreement providing such coverage. In COBRA, the Congress extended Medicare coverage (and the corresponding hospital insurance payroll tax) on a mandatory basis to State and local government employees hired after March 31, 1986, for services performed after that date.

Under present law, State and local government employees hired before April 1, 1986, are not covered under Medicare unless a voluntary agreement is in effect. Medicare coverage (and the hospital insurance payroll tax) is mandatory for Federal employees.

For wages paid in 1989 to Medicare-covered employees, the total hospital insurance tax rate is 2.9 percent of the first $48,000 of wages (Code secs. 3101, 3111, and 3121). One-half of this tax is paid by the employee and one-half by the employer.

President's Budget Proposal

The President's budget proposal would extend Medicare coverage on a mandatory basis to all employees of State and local governments not otherwise covered under present law, without regard to their dates of hire. These employees and their employers would become liable for the hospital insurance portion of the FICA tax, and the employees would earn credit toward Medicare eligibility based on their covered earnings.

This proposal would be effective on October 1, 1989.

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[4] The proposal does not discuss the treatment of IDCs under the present law corporate adjusted current earnings adjustment.

Prior Action

During the 99th Congress, the Senate amendment to H.R. 5300 (the Omnibus Budget Reconciliation Act of 1986) included a provision similar to the President's budget proposal. This provision was deleted from the legislation in conference.

This provision in the President's budget proposal also was included in President Reagan's budget proposals for fiscal years 1988, 1989, and 1990.

9. Elimination of Superfund Petroleum Tax Differential

Present Law

Superfund taxes of 8.2 cents per barrel for domestic crude oil and 11.7 cents per barrel for imported petroleum products (including crude oil) are imposed on the receipt of crude oil at a U.S. refinery, the import of petroleum products and, if the tax has not already been paid, on the use or export of domestically produced oil.

Domestic crude oil subject to tax includes crude oil condensate and natural gasoline, but not other natural gas liquids. Taxable crude oil does not include oil used for extraction purposes on the premises from which it was produced, or synthetic petroleum (e.g., shale oil, liquids from coal, tar sands, biomass), or refined oil.

Petroleum products that are subject to tax upon import include crude oil, crude oil condensate, natural and refined gasoline, refined and residual oil, and any other hydrocarbon product derived from crude oil or natural gasoline that enters the United States in liquid form.

The petroleum tax generally expires on December 31, 1991. The tax will terminate earlier than that date if cumulative Superfund receipts during the reauthorization period equal or exceed $6.65 billion, and under certain other conditions.

Canada, Mexico, and the European Community filed a formal complaint under the General Agreement on Tariffs and Trade ("GATT") after the Superfund tax on imported oil was raised above that on domestic oil by the Superfund Amendments and Reauthorization Act of 1986. A GATT panel convened to investigate the complaint concluded that the differential petroleum tax rate is contrary to the GATT, and the panel ruling was accepted unanimously by the GATT Council on June 17, 1987. Under GATT rules, the United States either must amend the Superfund tax or compensate the plaintiffs to avoid possible retaliation.

President's Budget Proposal

The President's budget proposes a revenue neutral change in the Superfund excise taxes on domestic crude oil and imported petroleum products (including crude oil): increasing the rate on domestic crude oil (presently 8.2 cents per barrel) and lowering, to an equal level, the rate on imported petroleum products (presently 11.7 cents per barrel).

Prior Action

This proposal was also included in President Reagan's proposed budgets for fiscal years 1989 and 1990.

10. Repeal of Tax Reduction Trigger for Airport and Airway Trust Fund Excise Taxes

Present Law

Excise taxes are imposed on air passenger tickets (8 percent), domestic air freight (5 percent), international passenger departures ($3), and fuels for noncommercial aviation (12 cents per gallon on gasoline and 14 cents per gallon on other fuels). The Airport and Airway Revenue Act of 1987 extended these taxes through December 31, 1990.

Revenues from the aviation excise taxes are transferred to the Airport and Airway Trust Fund to finance Federal airport and airway programs. The 1987 Act provides for an automatic 50-percent reduction in the aviation excise taxes (other than the $3 international departure tax) in calendar year 1990, if the total appropriations for fiscal years 1988 and 1989 for airport improvements, facilities and equipment, and research, engineering and development are less than 85 percent of the total amounts authorized for these programs for fiscal years 1988 and 1989.

President's Budget Proposal

The President's budget proposal would repeal the automatic 50-percent reduction in aviation taxes scheduled for January 1, 1990, because of the shortfall of appropriations relative to authorizations. (The CBO baseline budget assumes that the tax reduction trigger will be effective on January 1, 1990, because total appropriations for the aforementioned Trust Fund programs for fiscal years 1988 and 1989 are less than 85 percent of authorizations.)

Prior Action

President Reagan's proposal for fiscal year 1989 and fiscal year 1990 also proposed repeal of the automatic aviation tax reduction.

11. Permanent Extension of 3-Percent Telephone Excise Tax

Present Law

The Federal telephone excise tax is 3 percent on local and long distance telephone service and on teletypewriter exchange service. The telephone tax is scheduled to expire after December 31, 1990; the 3-percent rate has been in effect since January 1, 1983.

President's Budget Proposal

The President's budget proposal would extend permanently the Federal telephone excise tax at its current 3-percent rate.

Prior Action

The 3-percent tax rate was extended through 1990 in the Omnibus Budget Reconciliation Act of 1987.

12. User Fee/Tax for U.S. Travel and Tourism Administration

Present Law

There is no general excise tax on international travel to and from the United States. A $3 per person international departure tax is applicable, however, to certain international flights exempt from the 8-percent domestic passenger ticket tax as part of the funding for the Airport and Airway Trust Fund.

President's Budget Proposal

The President proposes to impose a Travel Facilitation Fee of $1 for each traveler arriving at ports of entry in the United States, its possessions, and its territories. The fee would be collected from airline and cruise ship carriers and would be used to fund existing and expanded programs of the U.S. Travel and Tourism Administration in Fiscal Year 1990 and beyond.

Prior Action

The same proposal was included initially in President Reagan's budget submitted to Congress for fiscal year 1988, and it has been resubmitted for fiscal years 1989 and 1990.

B. IRS Enforcement Funding Initiative

Present Law

In fiscal year 1988, the IRS had approximately 114,875 full-time equivalent employees with a total budget of about $5.3 billion.

President's Budget Proposal

The President's budget proposal would increase IRS funding for tax law enforcement. The budget documents do not specify the size of the increase in the budget or how the increase would be spent.

Prior Action

The same IRS enforcement initiative was included in President Reagan's budget proposal for fiscal year 1990. (This proposal appears to be different from the IRS enforcement funding proposals in the earlier budgets of President Reagan.)

C. Customs Service User Fee

Present Law

An *ad valorem* user fee is applied to all formal entries of merchandise imported for consumption, except entries from the Caribbean Basin, less developed countries, certain U.S. components, and articles returned. The fee, which currently is 0.17 percent of value, is intended to provide revenue equal to the costs of the Customs Service commercial operations. The fee is scheduled to expire after September 30, 1990.

In the Omnibus Budget Reconciliation Act of 1987, collections from the fee were reclassified as offsets to outlays, rather than as receipts. For imported goods made with U.S. components, the Act exempted only the value of the U.S. component from the fee, rather than the total value of the good. A ruling of the General Agreement on Tariffs and Trade (GATT) in 1987 found the *ad valorem* fee to be inconsistent with the GATT requirement that user fees not exceed the approximate cost of customs processing services rendered for particular entries. Correcting legislation is needed to make the user fee consistent with GATT requirements.

President's Budget Proposal

Legislation is to be proposed to substitute for the single *ad valorem* rate a transaction-based schedule of fees more closely related to the actual cost of processing individual types of entries to cover the actual costs of commercial operations.

Prior Action

A proposal was included in President Reagan's budget submitted for fiscal year 1989 to ensure that the *ad valorem* fee structure represents the costs of processing individual entries and that collections from the fee are reclassified as budget receipts.

D. Certain Other User Fees Classified As Budget Receipts

1. Nuclear Regulatory Commission Fees

Present Law

The Nuclear Regulatory Commission currently assesses fees on the owners of nuclear power plants. Operators of nuclear power plants are charged fees based upon the number of staff hours required to inspect the facilities. The fees recover the costs incurred in inspecting the facilities, but do not recover all of the costs involved in regulating nuclear power plants.

President's Budget Proposal

The President's budget proposal would increase the fees assessed on the owners of nuclear power plants to a level sufficient to recover 100 percent of the costs incurred in regulating the facilities.

This proposal would be effective on October 1, 1989.

Prior Action

An identical proposal was included in President Reagan's budget for fiscal year 1990. A provision to increase the user fees, though not to recover 100 percent of regulatory costs, was included in the President's budget for fiscal year 1989.

2. Federal Emergency Management Agency Fees

Present Law

The Federal Emergency Management Agency currently assesses no user fees in its capacity as regulator of evacuation plans of nuclear power plants.

President's Budget Proposal

The President's budget proposal would impose user fees on the owners of nuclear power plants sufficient to recover 100 percent of the costs incurred by the Federal Emergency Management Agency in its capacity as regulator of evacuation plans of nuclear power plants.

The proposal would be effective on October 1, 1989.

Prior Action

An identical proposal was included in President Reagan's budget for fiscal year 1990. A provision to increase the user fees, though not to recover 100 percent of regulatory costs, was included in the President's budget for fiscal year 1989.

3. Federal Marine Fishing Licenses and Fees

Present Law

There are no provisions in present law to fund the conservation and management of the federally managed marine fishing resources, whether through a required permit or an *ad valorem* fee on commercial sales.

There is a Sport Fish Restoration Account in the Aquatic Resources Trust Fund. Present law appropriates to the Sport Fish Restoration Account amounts equivalent to the amounts received in the Treasury from (a) the taxes imposed on sport fishing equipment, and (b) the import duties imposed on fishing tackle and yachts and pleasure craft under the Tariff Schedules of the United States. Amounts in the Sport Fish Restoration Account are available, as provided by appropriation Acts, to carry out the purposes of the Act entitled "An Act to provide that the United States shall aid the States in fish restoration and management projects."

President's Budget Proposal

The Administration is proposing that the costs associated with Federal efforts to conserve and manage U.S. marine fishery resources be borne by those who benefit directly from Federal fishery, research, conservation, and management services. The President's budget proposes a permit requirement and an *ad valorem* fee on commercial sales, which would apply only to those fishermen who fish in the fishery conservation zone (3 to 200 miles offshore) or who fish for federally managed species. These fees are proposed to become effective on and after January 1, 1990.

Prior Action

In budgets submitted for fiscal years 1989 and 1990, the Administration recommended the initiation of Federal marine fishing license fees for commercial and recreational fishing.

4. Coast Guard User Fees

Present Law

The Coast Guard provides various services to recreational and commercial boaters, including inspections, licenses, navigation aids, and search and rescue operations. These services are funded from general revenues.

President's Budget Proposal

A new Coast Guard user fee, collected from the sale of $25 decals to the approximately six million recreational and commercial boaters using U.S. waterways, is being proposed. In addition, processing fees for inspections and other specific services are proposed.

Prior Action

In the budget submitted for fiscal year 1988, a phased implementation of user fees for certain Coast Guard services was proposed. According to the proposal, fees for direct, transactional services, e.g., issuing licenses, would be set to recover the actual cost of providing the service. Additional fees to finance other Coast Guard services were to be set in proportion to the Coast Guard's cost of providing the service to each class of users, such as, recreational boaters, commercial operators, and deep sea and inland commercial users.

No fees were to be charged for core governmental functions carried out by the Coast Guard, that is, defense, law enforcement, and polar ice operations.

5. IRS Taxpayer Telephone Information Services Fee

Present Law

The IRS does not charge taxpayers a fee when the IRS answers taxpayers' questions about the tax law. In fiscal year 1988, the IRS answered 52.2 million telephone calls requesting information. Over 99 percent of these calls were toll-free to the taxpayer.

President's Budget Proposal

The President's budget proposes the imposition of a user fee on taxpayer telephone information services beginning in fiscal year 1991. The General Explanations of the President's Budget Proposals Affecting Revenues (prepared by the Treasury Department) states that a design evaluation (including an actual demonstration of the technologies and systems capabilities) will be conducted in 1989 and 1990.

Prior Action

President Reagan's budget for fiscal year 1990 also proposed imposition of a user fee on taxpayer telephone information services beginning in fiscal year 1991.

E. Other: Railroad Unemployment Compensation Fund Reimbursement to Amtrak

Present Law

The railroad unemployment and sickness benefit program is financed by payroll taxes paid by railroad employers. The employees themselves do not contribute. Currently, the taxable earnings base is the first $600 of each employee's monthly earnings. The payroll tax rate may vary from 0.5 percent to 8.0 percent as needed to meet liabilities.

The Technical and Miscellaneous Revenue Act of 1988 provided an exemption from the full railroad unemployment tax rate for public commuter railroads in 1989 and 1990. Such public commuter railroads will reimburse the unemployment system for the amount of benefits paid during the year to these employees. Starting in 1991, those railroads will again be subject to payroll taxes on the same basis as other railroads.

President's Budget Proposal

The President's budget proposal would extend the same reimbursable status to Amtrak as was extended to public commuter railroads.

This proposal would be effective for 1989 and 1990.

Prior Action

This provision in the President's budget proposal was also included in President Reagan's budget proposal for fiscal year 1990.

II. ADMINISTRATION'S ESTIMATED BUDGET EFFECTS OF REVENUE PROPOSALS

Fiscal Years 1989–1994

[Billions of Dollars]

Item	1989	1990	1991	1992	1993	1994
A. Tax Provisions:						
1. Capital gains tax rate reduction for individuals	0.7	4.8	4.9	3.5	2.2	−6.8
2. Proposed child tax credit and refundable child and dependent care tax credit [1]		(2)	(2)	(2)	−0.1	−0.1
3. Deduction for special needs adoption		(2)	(2)	(2)	(2)	(2)
4. Enterprise zone tax incentives		−0.2	−0.2	−0.3	−0.4	−0.5
5. Permanent tax credit for qualified research expenditures		−0.4	−0.7	−1.0	−1.2	−1.4
6. R&E expense allocation rules		−1.7	−0.7	−0.8	−0.9	−1.0
7. Energy tax incentives:						
a. 10% credit for exploratory drilling		−0.2	−0.3	−0.3	−0.4	−0.4
b. 10% credit for tertiary enhanced recovery		(2)	(2)	(2)	(2)	(2)
c. Eliminate the transfer rule and increase the net income to 100% for percentage depletion by independent producers and royalty owners		(2)	(2)	(2)	(2)	(2)
d. Eliminate 80% of exploratory IDC tax preferences from minimum tax for independent producers		−0.1	−0.1	−0.1	−0.1	−0.1
8. Medical hospital insurance (HI) for all State and local employees		1.8	1.9	1.9	1.9	1.9
9. Elimination of Superfund petroleum tax differential						
10. Repeal of Airport and Airway Trust Fund tax reduction trigger		0.9	1.6	1.7	1.8	1.9
11. Permanent extension of 3-percent telephone excise tax			1.6	2.6	2.8	3.0

12. User fee/tax for U.S. Travel and Tourism Administration		[3]	[3]	[3]	[3]	[3]
B. IRS Enforcement Funding Initiative		0.3	0.6	0.7	0.7	0.7
C. Customs Service User Fees			0.2	0.2	0.2	0.2
D. Certain Other User Fees Classified as Budget Receipts:						
1. Nuclear Regulatory Commission fees		0.3	0.3	0.3	0.3	0.3
2. Federal Emergency Management Agency fees		[3]	[3]	[3]	[3]	[3]
3. Federal marine fishing licenses and fees		[3]	0.1	0.1	0.1	0.1
4. Coast Guard boating fees		0.2	0.2	0.2	0.2	0.2
5. IRS telephone information service fee			[3]	[3]	[3]	[3]
E. Other: Railroad Unemployment Compensation Fund Reimbursement to Amtrak	[2]	[2]	[2]	[3]	[3]	[3]

[1] Refundable tax credits involving refunds which exceed tax liability are shown as increased outlays. Outlays will increase by $0.2 billion in FY 1990, $1.8 billion in FY 1991, $2.2 billion in FY 1992, $2.4 billion in FY 1993, and $2.8 billion in FY 1994.

[2] Loss of less than $50 million.

[3] Gain of less than $50 million.

Source: Department of the Treasury, Office of Tax Analysis.